

GEORGE WASHINGTON UNIVERSITY
Department of Economics

Topics in International Finance: Economics 293, Fall 2009

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Syllabus

I. Course Description

This course focuses on macroeconomic issues and policies in open economies. It begins with a review of a traditional model of an open economy under different exchange rate regimes. It continues with the study of some of the most relevant topics in international finance, such as, determinants of international capital flows, currency crises, financial contagion, current account sustainability and sovereign crises, fiscal problems, and macropolicies in emerging markets and mature economies. Based on this discussion, the course ends by revisiting the debate of fixed versus flexible exchange rate regimes. At this time, special attention is dedicated to the debate about dollarization and currency unions.

II. Examinations

Midterm: October 26, 2009

Final: December 14, 2009

III. Problem Sets and Presentation

There will be 4 problem sets, two before the midterm and the rest before the final. While problem sets are not required, it is advisable for students to do the problem sets so as to be prepared for the exams. Students will be required to make a 30-minute presentation on one of the topics of the course.

IV. Basis of Grades

The course grade will be based on: the midterm (30%), the final exam (40%), and class participation and presentation (30%).

Reading List

I. Fixed and Floating Exchange Rate Regimes: A Review

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapters 13, 14, 16 (pages 407-434), and 17 (pages 447-463).

II. International Capital Flows

Calvo, Guillermo, Leonardo Leiderman, and Carmen Reinhart, "Inflows of Capital to Developing Countries in the 1990s," *Journal of Economic Perspectives*, vol. 10, (2), Spring 1996, pages 123-139.

Calvo, G.A., L. Leiderman and C.M. Reinhart, "Capital Inflows and Real Exchange Rate Appreciation in Latin America: The Role of External Factors," IMF Staff Papers, 1993.

Claessens, S., M. Dooley, and A. Warner, 1995, "Portfolio Capital Flows: Hot or Cold?" *World Bank Economic Review*, 9, pages 153-174.

Christensen, Jakob, "Capital Inflows, Sterilization, and Commercial Bank Speculation: The Case of the Czech Republic in the Mid-1990s," IMF Working Paper WP/04/218, 2004.

De Gregorio, J., S. Edwards, and R. Valdes, "Controls on capital inflows: Do they work?" NBER Working Paper No. 7645, 2000.

Edwards, S. "How Effective are Capital Controls?" *The Journal of Economic Perspectives*, Vol. 13, No. 4. (Autumn, 1999), pp. 65-84.

Eichengreen, Barry, "Trends and Cycles in Foreign Lending," in Siebert, Horst, ed., *Capital Flows in the World Economy*, Tubingen: Mohr, 1991, pages 3-28.

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 21.

Kaminsky, G., and S. Schmukler, 2004, "Short-Run Pain, Long-Run Gain: Financial Liberalization and Stock Market Cycles, NBER Working Paper. Also in: <http://home.gwu.edu/~graciela>.

Kaminsky, G and A. Fostel, "Latin America Access to International Capital Markets: Good Behavior or Global Liquidity?"

Reinhart, C. and Reinhart, V., "Some Lessons for Policy Makers Dealing with the Mixed Blessing of Capital Inflows," in *Capital Flows and Financial Crises*, M. Kahler, ed (New York: Council on Foreign Relations, 1998), pages 93-127.

Also in <http://www.puaf.umd.edu/faculty/papers/reinhart/reinhart.htm>.

Reinhart, C. and Reinhart, V., "Capital Flow Bonanzas: An Encompassing View of the Past and Present," NBER Working Paper 14321, September 2008.

Reinhart, Carmen M. and Vincent R. Reinhart, "Capital Inflows and Reserve Accumulation: The Recent Evidence," NBER Working Paper 13842, March 2008.

Prasad, Ewar and Shang-Jin Wei, "The Chinese Approach to Capital Inflows: Patterns and Possible Explanations," International Monetary Fund Working Paper 05/79, April 2005. In <http://www.internationalmonetaryfund.com/external/pubs/ft/wp/2005/wp0579.pdf>

III. Crises

Agénor, P., Bhandari, J., and R. Flood, "Speculative Attacks and Models of Balance of Payments Crises," *IMF Staff Papers*, 39, 357-94.

Chiodo, Abigail and Michael T. Owayang, "A Case Study of a Currency Crisis: The Russian Default of 1998," Federal Reserve Bank of St. Louis, November/December 2002. Also in: <http://research.stlouisfed.org/publications/review/02/11/ChiodoOwyang.pdf>

Goldstein, Morris, Graciela Kaminsky, and Carmen Reinhart, *Assessing Financial Vulnerability: An Early Warning System for Emerging Markets*, Institute for International Economics, 2000. chapters 2, 3, and 5

Kaminsky, G. and C. Reinhart, "The Twin Crises: The Causes of Banking and Balance-of-Payments Problems," *American Economic Review*, June 1999. Also in <http://home/gwu.edu/~graciela>

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 17 (pages 460-463 and 482-484).

Obstfeld, M. "The Logic of Currency Crises," NBER Working Paper No. 4640 and *Cahiers Economiques et Monétaires*, 1994, 43, 189-213.

Diaz-Alejandro, C., "Good-Bye Financial Repression, Hello Financial Crash," *Journal of Development Economics*, 1985, 19.

McKinnon, R. and H. Pill, "Credible Liberalization and International Capital Flows: The Overborrowing Syndrome," in T. Ito and A. O. Krueger (eds) *Financial Deregulation and Integration in East Asia*, The University of Chicago Press, 1996.

Reinhart, Carmen M., Kenneth S. Rogoff, "Is The 2007 U.S. Subprime Crisis So Different? An International Historical Comparison," *American Economic Review*, May 2008.

Reinhart, Carmen M., Kenneth S. Rogoff, "The Aftermath of Financial Crises," *American Economic Review*, May 2009, 466-472.

Velasco, A. "Financial and Balance of Payments Crises," *Journal of Development Economics*, 1987, 27, pages 263-283.

IV. Contagion

Calvo, G., "Capital Flows and Capital-Market Crises: the Simple Economics of Sudden Stops," <http://www.bsos.umd.edu/econ/ciecalvo.htm>, June 1998.

Eichengreen, B., Rose, A.K. and Wyplosz, C., "Contagious Currency Crises," Centre for Economic Policy Research (London) Discussion Paper No. 1453, August 1996.

Glick, R., and A. K. Rose, "Contagion and Trade: Why Are Currency Crises Regional?" *Journal of International Money and Finance*, August 1999.

Kaminsky, G., and C. Reinhart, "On Crises, Contagion, and Confusion," *Journal of International Economics*, Vol. 51 No. 1, June 2000, 145-168.

Kaminsky, G. and C. Reinhart, "The Center and the Periphery: The Globalization of Financial Turmoil," mimeo March 2002.

Kaminsky, G., C. Reinhart, and C. Végh, "The Unholy Trinity of Financial Contagion" *Journal of Economic Perspectives*, Vol. 17, Issue 4, Fall 2003, 51-74.

Kaminsky, Graciela, Richard Lyons, and Sergio Schmukler, "Economic Fragility, Liquidity, and Risk: The Behavior of Mutual Funds during Crises," January 2000, in <http://gwu.edu/~graciela>.

Kaminsky, Graciela and Carmen Reinhart, "Bank Lending and Contagion: Evidence from the Asian Crisis," in Takatoshi Ito and Anne Krueger (eds), *Regional and Global Capital Flows: Macroeconomic Causes and Consequences*, (Chicago: University of Chicago Press for the NBER, 2001), 73-99. Also in <http://home.gwu.edu/~graciela>.

International Monetary Fund, *World Economic Outlook, International Financial Contagion*, Chapter III, May 1999, in <http://www.imf.org/external/pubs/ft/weo/1999/01/0599ch3.pdf>

V. Sovereign Crises, Models and Standard Approaches to Evaluate Debt Sustainability

Blanchard, O., Giavazzi, F. and F. Sa. 2005. "The U.S. Current Account and the Dollar," NBER Working Paper No. 11137, February Edwards, S. "Debt Relief and Fiscal Sustainability," NBER Working Paper No. 8939 May 2002.

Cooper, Richard N. 2008. "Global Imbalances: Globalization, Demography, and Sustainability," *Journal of Economic Perspectives*, 22(3): 93-112

- Dooley, Michael, David Folkerts-Landau, and Peter Garber, "Savings Gluts and Interest Rates: The Missing Link to Europe," National Bureau of Economic Research Working Paper No 11520, July 2005.
- Edwards, Sebastian, "Is the U.S. Current Account Deficit Sustainable? And if not, How Costly is Adjustment Likely to Be?" National Bureau of Economic Research Working Paper No. 11541, August 2005.
- Feldstein, Martin 2008. "Resolving the Global Imbalance: The Dollar and the U.S. Saving Rate." *Journal of Economic Perspectives*, 22(3): 113–25.
- Inter-American Development Bank, *Living with Debt*, 2007 Report.
- International Monetary Fund, World Economic Outlook, 2007, Chapter 3: Public Debt in Emerging Markets: Is it Too High? September.
- Krugman, P. 2000, "Crises: The Price of Globalization?" paper presented at the Federal Reserve Bank of Kansas City Symposium on *Global Opportunities and Challenges*, August 24-26, 2000, in <http://www.kc.frb.org/publicat/sympos/2000draft.htm>.
- Milesi-Ferretti, Gian Maria and Assaf Razin, "Current Account Reversals and Currency Crises: Empirical Regularities," in *Currency Crises* edited by Paul Krugman, Chicago: University of Chicago Press for NBER (also IMF Working Paper 98/89 in <http://www.imf.org>).
- Milesi-Ferretti, Gian Maria and Assaf Razin, "Current Account Sustainability," Princeton Studies in International Finance, 81, October 1996.
- Obstfeld, M. and K. Rogoff, 2000, "Perspectives on OECD Economic Integration: Implications for US Current Account Adjustment," paper presented at the Federal Reserve Bank of Kansas City Symposium on *Global Opportunities and Challenges*, August 24-26, 2000, in <http://www.kc.frb.org/publicat/sympos/2000draft.htm>.
- Obstfeld, Maurice and Kenneth Rogoff, 2005, "The Unsustainable US Current Account Position Revisited," National Bureau of Economic Research Working Paper No. 10869, October 2004.
- Taylor, A. M. "A Century of Current Account Dynamics." *Journal of International Money and Finance* 21 (November 2002): 725–48.
- Végh, C., *Open Economy Macroeconomics in Developing Countries*, MIT Press (forthcoming), Chapter 2. Pages: 18-25

VI. Evaluating Debt Sustainability under Uncertainty

Hostland and Karam, "Assessing Debt Sustainability in Emerging Market Economies, Using Stochastic Simulation Model", IMF Working Paper 05-226, December 2005. <http://www.imf.org/external/pubs/ft/wp/2005/wp05226.pdf>

García, M. and Rigobon, "A Risk Management Approach to Emerging Market's Sovereign Debt Sustainability with an Application to Brazilian Data," NBER Working Paper No. 10336, March 2004.

VII. Evaluating Debt Sustainability: Assets and Liabilities and Debt Intolerance

Inter-American Development Bank, *Living with Debt*, 2007 Report.

Alberola, E. and J. Montero, "Debt Sustainability and Procyclical Fiscal Policies in Latin America, Documentos de Trabajo No. 0611, 2006 Banco de España.

Mathisen and Pellechio, "Using the Balance Sheet Approach in Surveillance: Framework, Data Sources, and Data Availability", IMF Working Paper 06/100 <http://www.imf.org/external/pubs/ft/wp/2006/wp06100.pdf>

Reinhart, C., K. Rogoff and M. Savastano, "Debt Intolerance," *Brookings Papers on Economic Activity*, 2003, v2003(1), 1-74. Also in www.nber.org/papers/w9908.

Reinhart, C. and K. Rogoff, "Serial Default and The "Paradox" Of Rich To Poor Capital Flows," *American Economic Review* 94, May 2004.

Reinhart, C., "Default, Currency Crises, and Sovereign Credit Ratings," NBER Working Paper 8738. In <http://www.nber.org/papers/w8738>.

Reinhart, C. and K. Rogoff, "The Forgotten History of Domestic Debt," NBER Working Paper 13946, April 2008.

Ozler, Sule (1993) "Have Commercial Banks Ignored History?" *American Economic Review*, 83 (June) pages 608-20.

Mathisen and Pellechio, "Using the Balance Sheet Approach in Surveillance: Framework, Data Sources, and Data Availability", IMF Working Paper 06/100 <http://www.imf.org/external/pubs/ft/wp/2006/wp06100.pdf>

Sturzenegger and Zettelmeyer, "Haircuts: Estimating Investor Losses in Sovereign Debt Restructurings, 1998-2005", IMF Working Paper 05-137, July 2005. in <http://www.imf.org/external/pubs/cat/longres.cfm?sk=18271.0>

Jeanne, O. and A. Guscina, 2006, "Government Debt in Emerging Market Countries: A New Data Set," IMF Working Paper No. 06/98.

Jaimovich, D. and U. Panizza, 2006, "Public Debt Around the World: A New Dataset of Central Government Debt," Research Department Working Paper No. 561, Inter-American Development Bank.

Cowan, K. E. Levy-Yeyati, U. Panizza, and F. Sturzenegger, 2006, "Sovereign Debt in the Americas: New Data and Stylized Facts. Research Department Working Paper No. 577, Inter-American Development Bank.

Chinn, Menzie, and Jeffrey Frankel, "Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency?" National Bureau of Economic Research Working Paper No. 11510, July 2005.

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 20.

Obstfeld, M., J. C. Shambaugh, and A. M. Taylor. "The Trilemma in History: Tradeoffs among Exchange Rates, Monetary Policies, and Capital Mobility." *Review of Economics and Statistics* (2005).

VIII. Fiscal and Monetary Policies

Kaminsky, Graciela, Carmen Reinhart, and Carlos Végh, "When It Rains, It Pours: Procyclical Macropolicies and Capital Flows," in Mark Gertler and Kenneth S. Rogoff (eds.), *NBER Macroeconomics Annual 2004*, 11-53. NBER Working Paper 10780, September 2004. Also in <http://home/gwu.edu/~graciela>.

IX. Purchasing Power Parity and Real Exchange Rate Fluctuations

Bergin, Paul, Reuven Glick and Alan Taylor, "Productivity, Tradability, and the Long-Run Price Puzzle," National Bureau of Economic Research Working Paper No. 9739. 2003.

Chinn, Menzie, "A Primer on Real Effective Exchange Rates: Determinants, Overvaluation, Trade Flows, and Competitive Devaluations," National Bureau of Economic Research No. 11521, July 2005.

Froot, Kenneth and Kenneth Rogoff, 1995, "Perspective on PPP and Long-Run Real Exchange Rates," in *Handbook of International Economics*, G Grossman and K. Rogoff, eds, Amsterdam, North Holland, pages 1647-88, also in NBER Working Paper No. 4952, April 1996

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapters 15.

Lothian, James, 1990, "A Century Plus of Japanese Exchange Rate Behavior, Japan and the World Economy, 2, pages 47-50.

Taylor, Alan, A Century of Purchasing Power Parity, Review of Economics and Statistics, 84:1, pages 139-150, 2002.

X. Fixed Versus Floating Once More

Calvo, Guillermo and Carmen Reinhart, "Fear of Floating," University of Maryland, Working Paper, 2000, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>

Calvo, Guillermo and Carmen Reinhart, "When Capital Inflows Come to a Sudden Stop: Consequences and Policy Options," June 1999 University of Maryland, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>.

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Calvo, Guillermo and Carmen Reinhart, "Fixing for Your Life," August 2000, University of Maryland, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>